SUPERVISION GUIDELINE NO. 5

**ISSUED UNDER THE AUTHORITY OF PART IX, SECTION 61
OF THE FINANCIAL INSTITUTIONS ACT 1995,
(NO. 1 OF 1995)**

LOAN PORTFOLIO REVIEW, CLASSIFICATION, PROVISIONING, AND OTHER RELATED REQUIREMENTS

Issued :
· To all banks
Circular No. 48/96 June11, 1996
· To all non-banks
Circular No. 49/96 June 11, 1996

Bank of Guyana
June 11, 1996.

LOAN PORTFOLIO REVIEW

1. A licensed financial institution shall conduct a qualitative appraisal of its loan portfolio comprising all loans, overdrafts, receivables, and other extensions of credit at least twice yearly. The review shall include the loan portfolio of the trust department of a licensed financial institution authorised to engage in trust business.

2. A summary of the consolidated (Head/Main Office and branches) loan portfolio review as at June 30 of each year shall be submitted by a licensed financial institution to the Bank not later than the end of the succeeding month in the prescribed form (Schedule I). A separate loan portfolio review summary shall be submitted for the trust department. Each review shall cover at least seventy percent of the loan portfolio (excluding debt securities of the Government) and shall include the following -

   (a) large accounts above one percent of the loan portfolio, including aggregate loans to borrower groups;
   (b) all past-due accounts;
   (c) all non-performing accounts;
   (d) all identified problem accounts; and
   (e) large off-balance sheet commitments above one percent of the loan portfolio.

PAST-DUE AND NON-PERFORMING ACCOUNTS

3. A licensed financial institution shall report in its monthly statement of assets and liabilities the outstanding balance of its loan portfolio considered to be past-due and those considered to be non-performing. The principal balance outstanding (and not the amount of delinquent payments) shall be used in calculating the aggregate amount of past-due and of non-performing accounts.

4. An account shall be reported as past-due when -

   (a) for a loan or an account with fixed repayment dates -

      (i) principal or interest is due and unpaid for one month to less than three months; or
      (ii) interest charges for one to two months have been capitalised, refinanced, or rolled-over.

   (b) for an overdraft or an account without fixed repayment dates -

      (i) approved limit has been exceeded for one month to less than three months;
      (ii) credit line has expired for one month to less than three months;
      (iii) interest charges for one month to two months have not been covered by deposits; or
      (iv) the account had turnovers which did not conform to the business cycle.

5. An account reported as past-due shall be reclassified and reported as non-performing when -

   (a) for a loan or an account with fixed repayment dates -

      (i) principal or interest is due and unpaid for three months or more; or
      (ii) interest charges for three months or more have been capitalised, refinanced, or rolled-over.

   (b) for an overdraft or an account without fixed repayment dates -

      (i) approved limit has been exceeded for three months or more; or
      (ii) credit line has expired for three months or more; or
      (iii) interest charges for three months or more have not been covered by deposits; or
      (iv) the account has developed a hardcore which was not converted into a term loan after three months or more.

6. Interest should not be accrued on a non-performing account unless it is well-secured and full collection of arrears is expected within three months. Interest on loans to the Government and any other loans and overdrafts secured by cash, cash substitutes, government securities, or government guarantees, shall continue to accrue up to the limit of the said security.

7. A non-accrual account may be restored to accrual status when all arrears of principal and interest have been paid or when it otherwise becomes well-secured and full collection is expected within three months.

8. A “well-secured" account for the purpose of this Guideline means that the collateral is sufficient to protect the licensed financial institution from loss of principal and interest through its timely disposition under a forced liquidation programme. Sufficiency implies the existence of proper legal documentation, a net realisable market value which is adequate to cover the amount of principal and interest outstanding, as well as costs of collection, and the absence of prior liens on the collateral which would diminish its value or otherwise prevent the licensed financial institution from acquiring clear title. Collateral such as specialised manufacturing facilities and equipment for ongoing operations which involve large-scale employment of workers would not normally be considered well-secured because of the difficulties of actual foreclosure or of disposing of the collateral in a timely manner at values sufficient to protect the financial institution from loss. An account may also be considered as well-secured if the collateral includes irrevocable guarantees issued by first-class banks and other licensed financial institutions, multinational companies, and governments where the beneficiary or licensee has performed the financial analysis necessary to determine that the issuer is financially sound, well-capitalised, and able to pay the guarantee on demand. Such guarantees should be unconditional and payable upon the default of the borrower and should be properly acknowledged by the issuer through independent confirmation.

CLASSIFICATION CRITERIA

9. The loan portfolio shall be classified based on the review of the following information-

    (a) the original amount of the credit facility, terms, interest rate, current balance and status, and purpose of the credit facility;
    (b) the business of the borrower, balance sheets, income statements, cash flows and other financial data both on the business and the guarantors;
    (c) an evaluation of the project being financed;
    (d) the collateral taken including appraisals done once every two years, legal assignments, insurances among others;
    (e) track record of the borrower including the servicing of previous borrowings; and
    (f) if part of a group, the performance of credit accommodations to other members of the group.

10. The loan portfolio classification process provides a basis for determining an adequate level of loan loss provisioning. The criteria for each of the five classifications are set out below but the Bank is not precluded from requiring a more severe classification for an account if such is warranted, based upon any additional information. These criteria shall be used by a licensed financial institution for its loan portfolio review as at June 30 of each year and by the inspectors of the Bank for loan classification purposes.

11. The following are the five categories for classifying accounts in the loan portfolio - Pass, Special-Mention, Substandard, Doubtful and Loss. For purposes of classification, the hardcore of an overdraft facility shall refer to that portion of an overdraft which shows little or no turnover over a period of twelve consecutive months. When an account has more than one deficiency, the deficiency which attracts the lower classification category shall be considered.

Pass

All of the following -

(a) the financial condition of the borrower is sound;
(b) there is adequate documentation to support the granting of credit, such as current financial statements, cash flows, credit checks, and evaluation report on collateral held; and
(c) the collateral for the account is unimpaired and represents tangible security to cover the financial institution's exposure.

This classification would therefore be assigned to:

(a) a loan which is up-to-date in repayments;

(b) a loan with principal or interest due and unpaid for less than one month; and

(c) an overdraft -

(i) operating within the approved limit;
(ii) with unexpired credit line;
(iii) with interest charges covered by deposits; or
(iv) with no hardcore and showing turnovers which conform to the business cycle.

Special Mention (Potential Problem Credits)

Any one or more of the following -

(a) an account which is currently up-to-date but evidence suggests that certain factors could in the future affect the borrower's ability to service the account properly or impair the collateral;

(b) there is inadequate credit documentation or other deviations from prudent credit extension practices;

(c) collateral is not fully in place;

(d) an account which could deteriorate because of current market conditions affecting the sector or industry;

(e) a renegotiated account which is up-to-date in repayments and adequately secured for a minimum of one year after rescheduling and during which period there would have been no inherent weaknesses affecting repayment;

(f) for a loan or an account with fixed repayment dates when -

   (i) principal or interest is due and unpaid for one month to less than three months; or
   (ii) interest charges for one to two months have been capitalised, refinanced or rolled-over;

(g) for an overdraft or an account without fixed repayment dates when -

   (i) approved limit has been exceeded for less than one month; or
   (ii) credit line has expired for less than one month; or
   (iii) interest charge for one month has not been covered by deposits; or
   (iv) the account had turnovers which did not conform to the business cycle.

Substandard

Any one or more of the following -

(a) there are well-defined credit weaknesses, such as, shortfalls in the borrower's cash flow, several renewals with capitalisation of interest;

(b) the primary source of repayment is insufficient to service the debt and the financial institution will have to look at secondary sources, such as collateral or refinancing, for repayment;

(c) the well-secured portion of a loan or an overdraft which would otherwise have been classified as doubtful or loss;

(d) for a loan or an account with fixed repayment dates when -

  (i) principal or interest is due and unpaid for three months to less than six months; or
  (ii) interest charges for three to five months have been capitalised, refinanced or rolled-over;

(e) for an overdraft or an account without fixed repayment dates when -

  (i) approved limit has been exceeded for one month to less than three months; or
  (ii) credit line has expired for one month to less than three months; or
  (iii) interest charges for two months to three months have not been covered by deposits; or
  (iv) the account has developed hardcore which was not converted into a term loan after three months to less than six months.

Doubtful

Any one or more of the following -

(a) the collection of the debt in full is highly questionable or improbable;

(b) there is possibility of a loss, and some factors exist which could improve the situation;

(c) the unsecured portion of a loan or an account with fixed repayment dates when -

   (i) principal or interest is due and unpaid for six months to less than twelve months; or
   (ii) interest charges for six to eleven months have been capitalised, refinanced or rolled-over;

(d) the unsecured portion of an overdraft or an account without fixed repayment dates when -

   (i) approved limit has been exceeded for three months to less than six months; or
   (ii) credit line has expired for three months to less than six months; or
   (iii) interest charges for four months to five months have not been covered by deposits; or
   (iv) the account has developed hardcore which was not converted into a term loan after six months to less than twelve months.

Loss

Any one or more of the following -

(a) an account considered uncollectible;

(b) an account which may have some recovery value but it is not considered practical nor desirable to defer write off;

(c) an account classified as doubtful with little or no improvement over the twelve- month period it has been classified as such;

(d) the unsecured portion of a loan or an account with fixed repayment dates when -

   (i) principal or interest is due and unpaid for twelve months or more; or
   (ii) interest charges for twelve months or more have been capitalised, refinanced or rolled-over;

(e) the unsecured portion of an overdraft or an account without fixed repayment dates when -

   (i) approved limit has been exceeded for six months or more; or
   (ii) credit line has expired for six months or more; or
   (iii) interest charges for six months or more have not been covered by deposits; or
   (iv) the account has developed hardcore which was not converted into a term loan after twelve months or more.

PROVISIONING REQUIREMENT

11. An allowance for probable losses shall be set-up in the books and presented as a contra-asset account in the Statement of Assets and Liabilities based on the following minimum levels of provisioning for each of the classification categories -

Classification	**Level of Provision**
Pass	0%
Special Mention	0%
Substandard	
- *portion secured by cash, cash substitutes, government securities or government guarantees*	0%
- *others*	20%
Doubtful	50%
Loss	100%
General Provision (portion of loan portfolio not reviewed)	1%

12. If the provision for losses reflected in the books is less than the required provisioning, the deficiency shall immediately be taken up in the books.

However, the deficiency arising from the loan portfolio review to be conducted as at June 30, 1997 by a licensed financial institution, may be booked over a period of four years provided that at the end of two years, at least fifty percent of the total deficiency shall be met.

OTHER REQUIREMENTS

13. The hardcore of an overdraft facility shall be converted into a term loan which specifies a fixed repayment programme. To facilitate review of overdraft facilities, a licensed financial institution shall maintain an analysis sheet for each account showing monthly balances and a summary of movements indicating the total amount and number of deposits and withdrawals, and the accruals and repayments of interest charges.

14. A renegotiated loan is a loan which has been refinanced, rescheduled, rolled-over, or otherwise modified because of weaknesses in the borrower's financial position or the non- repayment of the debt as arranged and shall be subject to the following conditions-

    (a) the existing financial position of the borrower can service the debt under the new conditions;
    (b) an account classified as doubtful or loss shall not be renegotiated unless an up-front cash payment is made to cover, at the least, unpaid interest or there is an improvement in the collateral taken which will make the renegotiated account, including unpaid interest, a well-secured account;
    (c) a commercial loan shall not be renegotiated more than twice over the life of the original loan and mortgage or personal loan not more than twice in a five-year period; and
    (d) a renegotiated loan shall not be reclassified upward for a minimum of one year following the new arrangements.

15. An account shall be written-off three months after being classified as a loss unless it shows a definite and significant improvement which indicates recovery within the next six months. A record of bad debts written-off shall be maintained in a memorandum account for monitoring purposes.

TRANSITION PERIOD

16. A licensed financial institution shall have a period of one year from June 11, 1996 to bring itself into compliance with this guideline.

(Name of Licenced Financial Institution)

Schedule I

LOAN PORTFOLIO REVIEW SUMMARY

As at

(Amounts to the nearest thousand)

Date Due: ________________________

A. **Category**	**Pass**	**Special Mention**	**Sub-Standard**		**Doubtful**		**Loss**		**Total**
B. Percentage (%) Provisioning	0%	0%	0% Secured by cash, gov't securities etc.	20% Others	20% Well-secured portion	50% Others	20% Well-secured portion	100% Others	
C. 1. Total dollar amount of Loan Portfolio [Amount should tally with 2(a)+2(b)]									
2. (a) Amount Reviewed									
(b) Amount not Reviewed									
(c) Number of Accounts on Loan Portfolio									
(d) Number of Accounts Reviewed									
D. Total Classified Accounts									

E. 1. Required Provision for Losses [E(a)+E (b)]									
(a) Computed Provision (respective amounts indicated at row D multiply by respective percentage at row B)									
(b) General Provision [1% of 2(b)]									
F. Booked Provision for Losses									
G. (Excess/Deficiency) [Item D1-Item E]									

* The total amount classified as sub-standard includes the initially identified sub-standard accounts and the well-secured portions of accounts classified as doubtful or loss.

Certified correct ______________________________ ______________________________ ______________________________

Signiture over printed name | Position | Date